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KUANGCHI SCIENCE LIMITED

光啟科學有限公司

(Incorporated in Bermuda with limited liability)

(Stock Code: 439)

ANNOUNCEMENT OF INTERIM RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2016

INTERIM RESULTS HIGHLIGHTS

- The Group's revenue was HK\$311,992,000, representing an increase of 462% over the six-month period ended 30 June 2015.
- The Group's gross profit was HK\$196,277,000, representing an increase of 8.5 times over the six-month period ended 30 June 2015.
- Earnings before interest, tax, depreciation, amortisation, share-based payment was HK\$124,279,000. Profit for the period attributable to shareholders of the Company was HK\$105,529,000 and earnings per share was 1.85 HK cents.
- The "Future Technology Business", a principal business of the Group, grew healthily, and posted a revenue of HK\$284,732,000. Profit attributable by shareholders of the Company for the period was HK\$105,529,000, achieved a turnaround from the loss for the six-month period ended 30 June 2015. The growth in profit of the "Future Technology Business" was primarily contributed by the significant increase in sales of the "Cloud" of the Group.
- The Group's "Cloud" project panned out and has since operated well, with base technological institute constructed. The "Cloud" in Zunyi is planned to complete inspection this year and move forward to the research and development of the functional loading of the "Cloud". Besides, the "Cloud" projects have gradually started running in the PRC cities and have successively entered into the design and implementation stages.
- During the period, the Group finalised the design of the "Solar Ship" and started to build the prototype and conducted flying tests. The "KuangChi Martin Jetpack" started full safety tests and stepped further towards its commercial use.
- The Group began its design and development effort on the manned version of the "Traveller", the key project for the Group's near space business. The Group will seek to carry out the launch and recovery tests of the manned version of the "Traveller" in the second half of the year.

The board of directors (the “Board”) of KuangChi Science Limited (the “Company”) announces the unaudited interim results of the Company and its subsidiaries (the “Group”) for the six months ended 30 June 2016 (the “Period”) together with the comparative figures for the same period in 2015 (the “Comparative Period”) as follows:

**CONDENSED CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER
COMPREHENSIVE INCOME**

FOR THE SIX MONTHS ENDED 30 JUNE 2016

	<i>NOTES</i>	Six months ended 30 June	
		2016	2015
		<i>HK\$’000</i>	<i>HK\$’000</i>
		(unaudited)	(unaudited)
Revenue	3	311,992	55,537
Cost of sales		(115,715)	(34,939)
Gross profit		196,277	20,598
Other income	4	9,769	31,192
Other gains and losses	5	4,921	(13,005)
Share of results of associate		(1,010)	–
Impairment loss recognised in respect of goodwill	13	–	(13,501)
Selling and distribution expenses		(22,645)	(10,371)
Research and development expenses		(49,766)	(29,063)
Administrative expenses		(55,787)	(54,171)
Finance costs		(791)	(4,342)
Profit (loss) before tax		80,968	(72,663)
Income tax expense	6	(16,176)	(186)
Profit (loss) for the period	7	64,792	(72,849)

		Six months ended 30 June	
		2016	2015
<i>NOTES</i>		HK\$'000	HK\$'000
		(unaudited)	(unaudited)
Other comprehensive (loss) income			
Items that may be reclassified subsequently to profit and loss:			
Exchange differences on translating foreign operations		<u>6,158</u>	<u>(13,203)</u>
Total comprehensive income (expense) for the period		<u>70,950</u>	<u>(86,052)</u>
Profit (loss) for the period attributable to:			
Shareholders of the Company		<u>105,529</u>	<u>(65,094)</u>
Non-controlling interests		<u>(40,737)</u>	<u>(7,755)</u>
		<u>64,792</u>	<u>(72,849)</u>
Total comprehensive profit (loss) attributable to:			
Shareholders of the Company		<u>111,577</u>	<u>(69,961)</u>
Non-controlling interest		<u>(40,627)</u>	<u>(16,091)</u>
		<u>70,950</u>	<u>(86,052)</u>
Earnings (loss) per share			
Basic (HK cents per share)	9	<u>1.85</u>	<u>(1.66)</u>
Diluted (HK cents per share)		<u>1.17</u>	<u>(1.66)</u>

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AT 30 JUNE 2016

		30 June 2016	31 December 2015
	<i>NOTES</i>	HK\$'000	HK\$'000
		(unaudited)	(audited)
ASSETS AND LIABILITIES			
NON-CURRENT ASSETS			
Plant and equipment	10	142,997	124,477
Investment properties	10	13,700	13,700
Other intangible asset	11	157,314	147,470
Goodwill	12	71,746	71,746
Investment in an associate		3,280	4,290
Derivative financial assets	13	8,030	51,300
Deposits paid for acquisition of plant and equipment		21,040	31,474
Prepaid lease payments		88,631	91,749
Pledged deposit		–	143,280
Prepayment for advertising		8,271	11,940
Loan receivable	14	9,310	–
		524,319	691,426
CURRENT ASSETS			
Prepaid lease payments		2,343	2,357
Inventories		52,281	44,037
Trade and other receivables	15	605,254	358,061
Income tax recoverable		2,313	8,339
Time deposits		93,969	125,133
Bank balances and cash		1,187,896	1,228,556
		1,944,056	1,766,483
CURRENT LIABILITIES			
Trade and other payables	16	227,689	120,056
Income tax payable		18,951	14,589
Obligations under finance lease		–	233
– amount due within one year		–	–
Convertible debenture	17	6,396	5,569
		253,036	140,447
NET CURRENT ASSETS		1,691,020	1,626,036
TOTAL ASSETS LESS CURRENT LIABILITIES		2,215,339	2,317,462

		30 June 2016 HK\$'000 (unaudited)	31 December 2015 HK\$'000 (audited)
	<i>NOTES</i>		
NON-CURRENT LIABILITIES			
Bank borrowings	18	–	142,397
Deferred tax liabilities		<u>54</u>	<u>67</u>
		<u>54</u>	<u>142,464</u>
NET ASSETS		<u>2,215,285</u>	<u>2,174,998</u>
CAPITAL AND RESERVES			
Share capital – Ordinary shares	19	57,137	57,137
Share capital – Preferred shares	19	3,757	3,757
Reserves		<u>1,858,640</u>	<u>1,861,237</u>
Equity attributable to owners of the Company		1,919,534	1,922,131
Non-controlling interest		<u>295,751</u>	<u>252,867</u>
TOTAL EQUITY		<u>2,215,285</u>	<u>2,174,998</u>

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE SIX MONTHS ENDED 30 JUNE 2016

	Attributable to shareholders of the Company										Attributable to non-controlling interests				
	Share capital- Ordinary shares HK\$'000	Share capital- Preferred shares HK\$'000	Share premium HK\$'000	Share premium- preferred share HK\$'000	Capital reserve HK\$'000 (note a)	Contributed surplus HK\$'000 (note b)	Share-based payment reserve HK\$'000 (note c)	Exchange translation reserve HK\$'000	Accumulated losses HK\$'000	Subtotal HK\$'000	Share-based payment reserves of subsidiaries HK\$'000 (note d)	Convertible debenture equity reserve of a subsidiary HK\$'000 (note e)	Share of net assets of subsidiaries HK\$'000	Subtotal HK\$'000	Total HK\$'000
Balance at 1 January 2015 (audited)	34,061	10,733	1,908,327	–	17,900	103,941	18,138	(535)	(379,326)	1,713,239	–	–	5,002	5,002	1,718,241
Loss for the period	–	–	–	–	–	–	–	–	(65,094)	(65,094)	–	–	(7,755)	(7,755)	(72,849)
Other comprehensive expense for the period	–	–	–	–	–	–	–	(4,867)	–	(4,867)	–	–	(8,336)	(8,336)	(13,203)
Total comprehensive expense for the period	–	–	–	–	–	–	–	(4,867)	(65,094)	(69,961)	–	–	(16,091)	(16,091)	(86,052)
Recognition of share-based payment	–	–	–	–	–	–	25,952	–	–	25,952	1,596	–	–	1,596	27,548
Settlement of share subscription price	–	8,050	–	93,916	–	–	–	–	–	101,966	–	–	–	–	101,966
Issue of ordinary shares upon conversion of preferred share	13,416	(13,416)	93,916	(93,916)	–	–	–	–	–	–	–	–	–	–	–
Acquisition of subsidiaries	–	–	–	–	(24,201)	–	–	–	–	(24,201)	11,325	3,823	259,913	275,061	250,860
Balance at 30 June 2015 (unaudited)	47,477	5,367	2,002,243	–	(6,301)	103,941	44,090	(5,402)	(444,420)	1,746,995	12,921	3,823	248,824	265,568	2,012,563
Balance at 1 January 2016 (audited)	57,137	3,757	2,069,865	26,281	(6,301)	103,941	77,930	(61,165)	(349,314)	1,922,131	15,671	3,823	233,373	252,867	2,174,998
Profit for the period	–	–	–	–	–	–	–	–	105,529	105,529	–	–	(40,737)	(40,737)	64,792
Other comprehensive income for the period	–	–	–	–	–	–	–	6,048	–	6,048	–	–	110	110	6,158
Total comprehensive income for the period	–	–	–	–	–	–	–	6,048	105,529	111,577	–	–	(40,627)	(40,627)	70,950
Derivative financial assets derecognised upon exercise of the underlying options (note 13)	–	–	–	–	–	–	–	–	(61,016)	(61,016)	–	–	–	–	(61,016)
Change in shareholding in existing subsidiary	–	–	–	–	–	–	–	–	(82,392)	(82,392)	–	–	82,392	82,392	–
Recognition of share-based payment	–	–	–	–	–	–	29,234	–	–	29,234	1,119	–	–	1,119	30,353
Balance at 30 June 2016	57,137	3,757	2,069,865	26,281	(6,301)	103,941	107,164	(55,117)	(387,193)	1,919,534	16,790	3,823	275,138	295,751	2,215,285

Notes:

- The balance of capital reserve represents the capital reserve arising from the group restructuring which took place in 1992 and an option right arising from the acquisition of a subsidiary in 2015 as set out in note 20(b).
- The balance of contributed surplus arose as result of the Company's capital reduction exercises which took place in the financial years of 2003 and 2006.
- The balance of share-based payment reserve represents share options granted on 26 August 2014 and 30 September 2015.
- The balance of share-based payment reserves of subsidiaries represent share options granted by subsidiaries as set out in note 20(a) and 20(b).
- The balance of convertible debenture equity reserve of a subsidiary represents the equity element of convertible debenture issued by a subsidiary as set out in note 20(b).

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE SIX MONTHS ENDED 30 JUNE 2016

	Six months ended 30 June	
	2016	2015
	HK\$'000	HK\$'000
	(unaudited)	(unaudited)
NET CASH USED IN OPERATING ACTIVITIES	(36,153)	(137,763)
INVESTING ACTIVITIES		
Purchase of plant and equipment	(13,604)	(81,149)
Purchase of intangible assets	(9,060)	(2,062)
Proceeds from disposal of plant and equipment	387	280
Interest received	7,343	25,914
Loans advanced to potential investees	(19,740)	–
Placement of pledged deposits	–	(113,326)
Withdrawal of pledged deposits	143,277	–
Withdrawal of time deposits	140,674	–
Placement of time deposits	(109,510)	–
Release of deposit paid for acquisition of a company	–	135,200
Acquisitions of subsidiaries	–	19,755
NET CASH GENERATED BY (USED IN) INVESTING ACTIVITIES	139,767	(15,388)
FINANCING ACTIVITIES		
Proceeds from bank borrowings	–	142,397
Proceeds from issue of preferred shares	–	101,966
Advance from a related party	–	5,835
Repayment of principal for obligations under finance lease	(233)	(864)
Repayment of bank borrowings	(142,397)	–
NET CASH GENERATED BY (USED IN) FINANCING ACTIVITIES	(142,630)	249,334
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(39,016)	96,183
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	1,228,556	1,485,818
Effect of foreign exchange rate changes	(1,644)	(5,796)
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD, REPRESENTED BY BANK BALANCES AND CASH	1,187,896	1,576,205

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

FOR THE SIX MONTHS ENDED 30 JUNE 2016

1. BASIS OF PREPARATION

The condensed consolidated financial statements of KuangChi Science Limited (the “Company”) and its subsidiaries (collectively referred to as the “Group”) have been prepared in accordance with Hong Kong Accounting Standard (“HKAS”) 34 “Interim Financial Reporting” issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”) as well as with the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”).

2. PRINCIPAL ACCOUNTING POLICIES

The condensed consolidated financial statements have been prepared on the historical cost basis except for investment properties and derivatives financial assets which are measured at fair values.

The accounting policies and methods of computation used in the condensed consolidated financial statements for the six months ended 30 June 2016 are the same as those followed in the preparation of the Group’s annual consolidated financial statements for the year ended 31 December 2015.

In the current interim period, the Group has applied, for the first time, the following new amendments to Hong Kong Financial Reporting Standards (“HKFRSs”) issued by the HKICPA that are mandatorily effective for the current interim period:

Amendments to HKFRS 11	Accounting for Acquisitions of Interests in Joint Operations
Amendments to HKAS 1	Disclosure Initiative
Amendments to HKAS 16 and HKAS 38	Clarification of Acceptable Methods of Depreciation and Amortisation
Amendments to HKFRSs	Annual Improvements to HKFRSs 2012 – 2014 Cycle
Amendments to HKAS 16 and HKAS 41	Agriculture: Bearer Plants
Amendments to HKAS 27	Equity Method in Separate Financial Statements
Amendments to HKFRS 10, HKFRS 12 and HKAS 28	Investment Entities: Applying the Consolidation Exception

The application of the above new amendments to HKFRSs in the current interim period has had no material effect on the amounts reported in these condensed consolidated financial statements and/or disclosures set out in these condensed consolidated financial statements.

The Group has not early applied any new or revised standards or amendments to standards that have been issued at the date of these condensed consolidated financial statements are authorised for issuance but are not yet effective.

3. SEGMENT INFORMATION

The following is an analysis of the Group’s revenue and results by reportable and operating segment:

	Future technology business (note)		Paper business		Property investment		Total	
	Six months ended 30 June		Six months ended 30 June		Six months ended 30 June		Six months ended 30 June	
	2016	2015	2016	2015	2016	2015	2016	2015
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Revenue	284,732	20,141	27,080	35,220	180	176	311,992	55,537
Segment profit (loss)	107,833	(23,000)	(6,400)	(26,849)	163	167	101,596	(49,682)
Unallocated corporate income							7,615	30,563
Unallocated corporate expenses							(27,452)	(49,202)
Finance costs							(791)	(4,342)
Profit (loss) before tax							80,968	(72,663)

Note: The novel space service segment is recorded as the future technology business segment in the current period.

The accounting policies of the operating segments are the same as the Group's accounting policies.

Segment profit(loss) represents the profit earned by (loss from) each segment without allocation of central corporate income and expense, directors' remuneration, financial advisory expenses, certain share-based payments, certain other income, and finance costs. This is the measure reported to the executive directors for the purposes of resource allocation and performance assessment.

Segment assets and liabilities

The following is an analysis of the Group's assets and liabilities by reportable and operating segments:

Segment assets

	30 June 2016 HK\$'000	31 December 2015 HK\$'000
Future technology business	1,112,267	818,060
Paper business	45,550	61,341
Property investment	13,705	13,705
	<hr/>	<hr/>
Total segment assets	1,171,522	893,106
Unallocated corporate assets	1,296,853	1,564,803
	<hr/>	<hr/>
Consolidated assets	2,468,375	2,457,909
	<hr/> <hr/>	<hr/> <hr/>

Segment liabilities

	30 June 2016 HK\$'000	31 December 2015 HK\$'000
Future technology business	225,447	109,061
Paper business	26,554	33,625
Property investment	100	93
	<hr/>	<hr/>
Total segment liabilities	252,101	142,779
Unallocated corporate liabilities	989	140,132
	<hr/>	<hr/>
Consolidated liabilities	253,090	282,911
	<hr/> <hr/>	<hr/> <hr/>

For the purposes of monitoring segment performance and allocating resources between segments:

- all assets are allocated to operating segments other than pledged deposit, time deposit, bank balances and cash and other assets for corporate use including certain plant and equipment, deposits and other receivables; and
- all liabilities are allocated to operating segments other than bank borrowing, deferred tax liabilities, obligations under finance lease and certain other payables.

4. OTHER INCOME

	Six months ended 30 June	
	2016	2015
	HK\$'000	HK\$'000
Sales of scrap materials	159	329
Interest income earned on bank balances and pledged deposit	7,343	30,338
Management fee income (<i>note</i>)	–	300
Sundry income	2,267	225
	<u>9,769</u>	<u>31,192</u>

Note: For the six months ended 30 June 2015, the amount represented income from administrative services provided to a related company, New Spring Label & Packaging Limited (“New Spring Label”), of which Mr. Ng Man Chan (“Mr. Ng”), a director of a number of subsidiaries of the Company, and Ms. Li Mi Lai (“Ms. Li”), a close family member of Mr. Ng, are controlling shareholders.

5. OTHER GAINS AND LOSSES

	Six months ended 30 June	
	2016	2015
	HK\$'000	HK\$'000
Loss on disposal of plant and equipment	(795)	(928)
Impairment loss recognised in respect of plant and equipment	–	(2,155)
Gain (loss) from changes in fair value of derivative financial assets (<i>note 13</i>)	17,746	(4,963)
Exchange loss, net	(11,840)	(4,959)
Others	(190)	–
	<u>4,921</u>	<u>(13,005)</u>

6. INCOME TAX EXPENSE

	Six months ended 30 June	
	2016	2015
	HK\$'000	HK\$'000
The charge comprises:		
Current tax		
PRC Enterprise Income Tax	16,189	–
Hong Kong profits tax	–	186
	<u>16,189</u>	<u>186</u>
Deferred taxation	(13)	–
	<u>16,176</u>	<u>186</u>

Hong Kong Profits Tax is calculated at 16.5% of the estimated assessable profit for the period.

PRC subsidiaries are subject to PRC Enterprise Income Tax at rate at 25% for the period (period ended 30 June 2015: 25%), except for a PRC subsidiary established in Qianhai which is subject to PRC Enterprise Income Tax at rate at 15% for the period (period ended 30 June 2015: 15%).

7. PROFIT (LOSS) FOR THE PERIOD

Six months ended 30 June
2016 2015
HK\$'000 HK\$'000

Profit (loss) for the period has been arrived at after charging:

Staff costs and directors' emoluments:

Staff costs:

Salaries and other benefits	56,386	18,104
Share-based payments	21,238	18,270
Contributions to retirement benefit	4,945	1,775
	<u>82,569</u>	<u>38,149</u>

Directors' emoluments:

Fees and other benefits	2,799	1,993
Share-based payments	9,115	9,278
	<u>11,914</u>	<u>11,271</u>
	<u>94,483</u>	<u>49,420</u>

Amortisation for intangible assets	7,499	2,876
Depreciation for plant and equipment	4,668	2,431
Financial advisory and legal fee	<u>2,515</u>	<u>14,500</u>

8. DIVIDEND

No dividends were paid, declared or proposed during the six months ended 30 June 2016 (six months ended 30 June 2015: nil). The directors of the Company have resolved not to declare any dividend for both of the interim periods.

9. EARNINGS (LOSS) PER SHARE

The calculation of the basic and diluted earnings (loss) per share attributable to the owners of the Company is based on the following data:

Six months ended 30 June
2016 2015
HK\$'000 HK\$'000

Profit (loss)		
Profit (loss) for the purpose of basic and diluted earnings (loss) per share (profit (loss) for the period attributable to shareholders of the Company)	105,529	(65,094)
Effect of dilutive potential ordinary shares:		
Adjustment to the share of losses of subsidiaries based on dilution of their earnings per share in relation to the Conversion Rights (as defined in note 20)	<u>(33,782)</u>	<u>—</u>
Profit (loss) for the purpose of diluted earnings per share	<u>71,747</u>	<u>(65,094)</u>

	Six months ended 30 June 2016	2015
Number of shares		
Weighted average number of ordinary shares for the purpose of basic earnings (loss) per share	5,713,734,459	3,932,356,927
Effect of dilutive potential ordinary shares:		
Preferred shares	375,666,666	–
Share options of the Company	23,096,051	–
	<u>6,112,497,176</u>	<u>3,932,356,927</u>
Weighted average number of ordinary shares for the purpose of diluted earnings (loss) per share		
	<u>6,112,497,176</u>	<u>3,932,356,927</u>

For the six months ended 30 June 2016, the computation of diluted earnings for share does not assume the conversion of a subsidiary's outstanding convertible debenture, or the exercise of the outstanding share options issued by loss-making subsidiaries of the Group since their assumed conversion or exercise would result in an increase in the earnings per share.

For the six months ended 30 June 2015, the computation of diluted loss per share does not assume the conversion of the Company's outstanding preferred shares, the subsidiary's convertible debenture, the exercise of the Company's and the subsidiaries' outstanding share options nor the exercise of the MACL Conversion Rights since their conversion or exercise would result in a decrease in loss per share.

10. MOVEMENTS IN PLANT AND EQUIPMENT AND INVESTMENT PROPERTIES

During the six months ended 30 June 2016, the Group acquired property, plant and equipment of approximately HK\$24,038,000 (six months ended 30 June 2015: HK\$63,088,000).

Certain construction in progress, amounting to approximately HK\$38,214,000, as at 31 December 2015 has been reclassified to other intangible assets because they were research and development costs capitalised for technical knowhow.

In addition, the Group acquired plant and equipment through the acquisitions of subsidiaries of approximately HK\$11,170,000 during the six months ended 30 June 2015 as set out in note 20.

During the six months ended 30 June 2016, the Group disposed of certain machineries with an aggregate carrying amount of approximately HK\$1,182,000 (six months ended 30 June 2015: HK\$1,208,000) for cash proceeds of HK\$387,000 (six months ended 30 June 2015: HK\$280,000), resulting in a loss on disposal of approximately HK\$795,000 (six months ended 30 June 2015: loss of HK\$928,000).

During the six months ended 30 June 2016, the Group carried out a review of the recoverable amount of the plant and machinery in the paper business segment. The review led to no impairment loss (six months ended 30 June 2015: HK\$2,155,000) being recognised. The recoverable amount of the relevant assets has been determined on the basis of their value in use. The discount rate used in measuring value in use was 11.19% per annum (six months ended 30 June 2015: 11.19%).

The fair value of investment property was determined based on the direct comparison method, where the value is assessed by reference to the comparable properties of similar size, character and location, factoring in all the respective advantages and disadvantages of each property. There has been no change from the valuation technique used in the comparative period.

The key input used in valuing the investment property is price per square foot. A slight increase in the price per square foot will increase significantly the fair value of the investment property and vice versa. Details of the Group's investment property and information about the fair value hierarchy as at 30 June 2016 is as follows:

	Level 3 HK\$'000	Fair values as at 30 June 2016 HK\$'000
Residential premise located in Hong Kong – level 3	<u>13,700</u>	<u>13,700</u>

The valuation as at 30 June 2016 was not carried out by independent qualified valuer. The fair value of the investment property of the Company as at 30 June 2016 is based on the directors' estimation with reference to the available market information.

There were no transfers into or out of Level 3 during the period.

11. OTHER INTANGIBLE ASSET

During the six months ended 30 June 2016, the Group capitalised development costs in other intangible assets of approximately HK\$9,060,000 (six months ended 30 June 2015: HK\$2,062,000). The amortisation of the other intangible assets during the six months ended 30 June 2016 amounts to approximately HK\$7,499,000 (six months ended 30 June 2015: HK\$2,778,000).

Certain construction in progress, amounting to approximately HK\$38,214,000, as at 31 December 2015 have been reclassified to other intangible assets because they were research and development costs capitalised for technical knowhow.

In addition, the Group acquired other intangible assets through the acquisitions of subsidiaries of approximately HK\$126,326,000 during the six months ended 30 June 2015 as set out in note 20.

12. GOODWILL

	<i>HK\$'000</i>
COST	
At 1 January 2015	84,054
Addition arising from acquisition of subsidiaries (<i>note 20</i>)	71,746
	<hr/>
At 31 December 2015 and 30 June 2016	155,800
IMPAIRMENT	
At 1 January 2015	70,553
Impairment loss recognised in the year	13,501
	<hr/>
At 31 December 2015 and 30 June 2016	84,054
	<hr/>
CARRYING VALUES	
At 30 June 2016	71,746
	<hr/> <hr/>
At 31 December 2015	71,746
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For the purposes of impairment testing, goodwill has been allocated to three individual cash generating units ("CGU"), being 3 groups of subsidiaries operating in (1) paper business; (2) development and commercialisation of jetpack products and (3) development and commercialisation of solar powered aircrafts, respectively.

The carrying amounts of goodwill (net of accumulated impairment losses) as at 30 June 2016 allocated to these 3 CGUs are as follows:

	30 June 2016 <i>HK\$'000</i>	31 December 2015 <i>HK\$'000</i>
Paper business	—	—
Development and commercialisation of jetpack products	32,364	32,364
Development and commercialisation of solar powered aircrafts	39,382	39,382
	<hr/>	<hr/>
	71,746	71,746
	<hr/> <hr/>	<hr/> <hr/>

The Group conducted impairment review on goodwill attributable to CGU operating in paper business at the end of the reporting period by reference to its estimated recoverable amount. The recoverable amount of the CGU has been determined based on a value-in-use calculation. Impairment loss amounting to approximately HK\$13,501,000 was recognised in respect of the CGU operating in paper business during the six months ended 30 June 2015 due to the continuous deterioration of industrial performance. The recoverable amount of the CGU, determined by using value-in-use, was HK\$39,424,000. The impairment calculation used cash flow projections based on financial budgets approved by the directors of the Company covering a five-year period, with pre-tax discount rate of 11.19%. The cash flows beyond the five-year period were extrapolated using a steady growth rate of 3%. The growth rate was based on the relevant industry growth rate forecast and does not exceed the average long-term growth rate for the relevant industry. The key assumptions for the value-in-use calculation related to the estimation of cash flows included gross margin and discount rate. Gross margin represents budgeted gross margin, which is based on past performance and the management's expectation for the market development. The discount rate used is pre-tax rates that reflect current market assessments of the risks specific to the relevant industry.

The Group also conducted impairment reviews on goodwill attributable to CGUs operating in development and commercialisation of jetpack products business ("Jetpack CGU") and solar powered aircrafts business ("Aircrafts CGU") at the end of the reporting period by reference to respective CGU's value-in-use and assessed that no impairment was necessary. The impairment calculation used cash flow projections based on financial budgets approved by the directors of the company covering a 5-year period for Jetpack CGU and Aircrafts CGU, with post-tax discount rate of 18% (31 December 2015: 17.95%) for Jetpack CGU and 23% (31 December 2015: 24.08%) for Aircrafts CGU. The cash flows beyond the 5-year period were extrapolated using a steady growth rate of 2% (31 December 2015: 2%) for both Jetpack CGU and Aircrafts CGU. The growth rate was based on the relevant industry growth rate forecast and does not exceed the average long-term growth rate for the relevant industry.

The key assumptions for the value-in-use ("VIU") calculation related to the estimation of cash flows included gross margin and discount rate. Gross margin represents budgeted gross margin, which is based on the management's expectation for the market development. The discount rate used is post-tax rates that reflect current market assessments of the risks specific to the relevant industry.

The following table illustrates the effect on VIU of reasonably possible changes to key assumptions for Jetpack CGU and Aircrafts CGU respectively. This reflects the sensitivity of VIU to each key assumption on its own and it is possible that more than one favourable and/or unfavourable change will occur at the same time. The directors of the Company consider that a reasonably possible unfavourable change in key assumptions will not lead to the goodwill impairment losses. However, as both of the CGUs are in development stage, a significant unfavourable change in any of the key assumptions could cause an impairment loss to be recognised in respect of these CGUs.

Jetpack CGU – Martin Aircraft Company Limited (“MACL”)

	Favourable change	Unfavourable change
At 30 June 2016		
Perpetual growth rate (current model: 2%)	+1%	–1%
Increase (decrease) in VIU (HK\$’000)	17,468	(15,585)
Discount rate (current model: 18%)	–10% to 16.20%	+10% to 19.80%
Increase (decrease) in VIU (HK\$’000)	108,993	(80,513)
At 31 December 2015		
Perpetual growth rate (current model: 2%)	+1%	–1%
Increase (decrease) in VIU (HK\$’000)	5,809	(5,179)
Discount rate (current model: 17.95%)	–10% to 16.16%	+10% to 19.74%
Increase (decrease) in VIU (HK\$’000)	26,210	(20,170)

Aircrafts CGU – Solar Ship Inc. (“Solar Ship”)

	Favourable change	Unfavourable change
At 30 June 2016		
Perpetual growth rate (current model: 2%)	+1%	–1%
Increase (decrease) in VIU (HK\$’000)	6,250	(5,688)
Discount rate (current model: 23%)	–10% to 20.70%	+10% to 25.30%
Increase (decrease) in VIU (HK\$’000)	30,441	(23,960)
At 31 December 2015		
Perpetual growth rate (current model: 2%)	+1%	–1%
Increase (decrease) in VIU (HK\$’000)	3,579	(3,275)
Discount rate (current model: 24.08%)	–10% to 21.68%	+10% to 26.49%
Increase (decrease) in VIU (HK\$’000)	19,973	(15,512)

13. DERIVATIVES FINANCIAL ASSETS

	Derivative – share swap HK\$’000	Derivative – subscription right of convertible securities HK\$’000	Total HK\$’000
Recognition on acquisition of subsidiaries on 23 February 2015 (<i>note 20</i>)	20,350	31,613	51,963
Change in fair value	(234)	(429)	(663)
Carrying value at 31 December 2015	20,116	31,184	51,300
Change in fair value	10,310	7,436	17,746
Derecognised upon exercise of underlying options	(22,396)	(38,620)	(61,016)
Carrying value at 30 June 2016	8,030	–	8,030

During the year ended 31 December 2015, the Group entered into an investment agreement with MACL (refer to note 20(a)). The agreement contains derivatives that are measured at FVTPL. During the six months ended 30 June 2016, gain from changes in fair value of share swap and subscription right of convertible securities amounted to HK\$10,310,000 and HK\$7,436,000 respectively (for the year ended 31 December 2015: loss of HK\$234,000 and HK\$429,000) respectively.

On 29 February 2016, the Company exercised its right to subscribe for the entire convertible securities in MACL for AUD23,020,000 (equivalent to HK\$129,988,000) and immediately fully converted them into new ordinary shares of MACL. In addition, on the same date, the Company exercised 90% of the share swap to sell 45.9% of the equity interests in HKCo (as defined in note 20 (a)) to MACL in return for the allotment of 89,445,000 MACL shares. Immediately after the subscription and conversion of the convertible securities in MACL and exercise of the share swap, the Group held in aggregate 52.01% of issued share capital of MACL. The Company shall have the right to exercise the remaining 10% of the share swap prior to 22 August 2017. Since both MACL and HKCo were subsidiaries of the Group before these transactions, and they remain as subsidiaries of the Group after these transactions, are treated as equity transactions which resulted an adjustment between non-controlling interest and accumulated losses. The portion of derivative asset was exercised was derecognised at their fair value on exercise date and charged against accumulated loss. There is no impact on the condensed consolidated statement of profit or loss and other comprehensive income.

14. LOAN RECEIVABLE

The amount is an advance to a potential investee. It is unsecured, interest bearing at 7% per annum and repayable within 2 years from agreement date. Accordingly to the terms of the loan agreement, the Group has the right to convert the loan into the potential investee's shares at any prior to the maturity of the loan if the potential investee consummates certain transactions as stipulated in the loan agreement, at a certain discount to the subscription price to be paid by the other investors for these transaction. As the loan contains an embedded conversion option, the embedded conversion option is accounted for as a separate derivative as it meets the definition of a derivative, the risks and characteristics are not closely related to those of the loan and the loan is not measured at fair value through profit or loss.

The directors of the Company consider that the fair value of this derivative cannot be reliably measured because it is dependent on the share price to be paid by investors which is not stipulated in the loan agreement.

15. TRADE AND OTHER RECEIVABLES

The Group allows an average credit period to its customers as follows:

- Future technology business segment: 5 months to 10 months
- Paper business segment: 30 to 60 days
- Property investment segment: no credit period – payment of rental in advance

The following is an aged analysis of trade receivables presented based on the invoice date which approximates the respective revenue recognition date, at the end of the reporting period.

	30 June 2016 HK\$'000	31 December 2015 HK\$'000
Trade receivables		
0 – 30 days (<i>note a</i>)	353,573	297,995
31 – 60 days	1,720	9,637
61 – 90 days	1,268	1,681
91 – 180 days	914	1,129
181 – 365 days (<i>note b</i>)	189,712	4
	547,187	310,446
Deposits and other receivables (<i>note c</i>)	22,747	11,994
Interest receivables	2,318	10,906
Prepayment for advertising	6,235	11,978
Other prepayments	26,767	12,737
	605,254	358,061

Notes:

- a. As at 30 June 2016, amount includes trade receivables from sales of the “Cloud”, a flying apparatus platform amounting to approximately HK\$333,136,000 (equivalent to RMB285,000,000) of which HK\$14,028,000 (RMB12,000,000) was past due and subsequently settled subsequently in August 2016. The remaining HK\$319,108,000 (equivalent to RMB273,000,000) was not yet due. As at 31 December 2015, amount includes trade receivables from sales of the “Cloud” amounting to approximately HK\$286,202,000 (equivalent to RMB 239,700,000) which was not yet due.
- b. Amount includes trade receivables due from customers who are government related bodies, amounting to approximately HK\$189,712,000 (equivalent to RMB162,300,000) (2015: Nil). There was a delay on settlement mainly due to the stringent governmental internal procedure for funding application. These customers have provided repayment schedules to the Company and committed to settle the outstanding balances according to the repayment schedules. The management is of the view that these customers have solid financial background and therefore no recoverability issue on these receivables is expected.
- c. Deposits and other receivables mainly include an advance to the shareholder of a potential investee amounting to HK\$10,430,000 (2015: Nil). The amounts are secured by the equity interests of a private company held by such shareholder, interest bearing at 8% per annum and repayable within one year from the agreement date.

16. TRADE AND OTHER PAYABLES

The following is an aged analysis of trade payables presented based on the invoice date at the end of the reporting period.

	30 June 2016 HK\$'000	31 December 2015 HK\$'000
Trade payables		
0 – 90 days	16,090	16,480
Over 90 days	1,574	3,832
	17,664	20,312
Deposit received	1,261	536
Other payables and accruals (<i>note a</i>)	26,235	45,677
Accrued salary	29,269	15,090
Other tax payables (<i>note b</i>)	83,396	38,441
Deferred revenue (<i>note c</i>)	69,864	–
	227,689	120,056

Notes:

- a. As at 30 June 2016, the balance of other payables and accruals includes approximately HK\$5,877,000 (31 December 2015: HK\$13,742,000) due to Mr. Ng. The amount is unsecured, interest-free and repayable on demand.
- b. Other tax payables mainly include value-added tax payables amounting to HK\$73,062,000 (2015: HK\$32,619,000) for revenue generated from Future technology business.
- c. During the six months ended 30 June 2016, the Group received a conditional government grant amounting to RMB60,000,000 (equivalent to HK\$69,864,000) from a city government in China to develop and promote the commercialisation of innovative technology. As at 30 June 2016, the government grant has been recognised as deferred income as the government's assessment attaching to the government grant is still carrying out. Since the government grant is for research and development purpose, it is classified as operating cash flows in the condensed consolidated statement of cash flows.

All Group's trade payables are denominated in the functional currency of the group entities.

The average credit period on purchase of goods is 90 days. The Group has financial risk management policies in place to ensure that all payables are settled within the credit timeframe.

17. CONVERTIBLE DEBENTURE

This represents an unsecured convertible debenture issued by Solar Ship. The convertible debenture is denominated in Canadian dollars ("CAD"), outstanding with par value of CAD1,000,000 (equivalent to approximately HK\$5,998,000) bearing interest at 12% per annum and maturing in November 2016. The convertible debenture holders are entitled to convert the convertible debenture into common shares of Solar Ship at a price of CAD100 per share.

The convertible debenture contain two components, liability and equity elements. The equity element is presented in equity heading "equity component of convertible debenture of a subsidiary". The effective interest rate of the liability component is 14% per annum.

18. BANK BORROWINGS

	30 June 2016 HK\$'000	31 December 2015 HK\$'000
Secured borrowings repayable more than two years but not more than five years (<i>note</i>)	—	142,397

Note: As at 31 December 2015, borrowings carried interest at three-month HIBOR plus a margin of 2.8% which was approximately 3.19% and were secured by pledged deposits. During the six months ended 30 June 2016, the bank borrowings were fully repaid.

19. SHARE CAPITAL

Ordinary shares	Number of shares	Equivalent to HK\$'000
Authorised:		
Ordinary shares of HK\$0.01 each		
At 1 January 2015, 31 December 2015 and 30 June 2016	7,316,666,668	73,167
Issued and fully paid:		
At 1 January 2015	3,406,067,793	34,061
Issue of ordinary shares upon conversion of preferred shares (<i>note</i>)	2,307,666,666	23,076
At 31 December 2015 and 30 June 2016	5,713,734,459	57,137

Preferred shares	Number of shares	Equivalent to HK\$'000
Authorised:		
Ordinary shares of HK\$0.01 each		
At 31 December 2014, 2015 and 30 June 2016	2,683,333,332	26,833
Issued and partially paid each:		
At 1 January 2015	2,683,333,332	10,733
Settlement of remaining share subscription price	–	16,100
Conversion of preferred shares (<i>note</i>)	(2,307,666,666)	(23,076)
Issued and fully paid of HK\$0.01 each		
At 31 December 2015 and 30 June 2016	375,666,666	3,757

Note: On 29 May 2014, the Company and certain subscribers (“Subscribers”) entered into a subscription agreement (“Subscription Agreement”), pursuant to which the Subscribers have conditionally agreed to subscribe for, and the Company has conditionally agreed to allot and issue, a total of 1,666,666,668 new ordinary shares and 2,683,333,332 new preferred shares (“preferred shares”).

During the year ended 31 December 2015, the Group received notices from the Subscribers to convert 2,307,666,666 fully paid preferred shares into ordinary shares. The amount transferred from preferred share capital to ordinary share capital was approximately HK\$23,076,000. At the same time, HK\$161,538,000 was transferred from the share premium-preferred share account to the share premium-ordinary share account.

20. ACQUISITION OF SUBSIDIARIES

Subsidiaries acquired

During the six months ended June 2015, for the purpose of business expansion, the Group has acquired controlling interests in the following entities, which have been accounted for using acquisition method:

	Principal activity	Place of incorporation/ operations	Class of shares held	Paid up issued share capital	Proportion of ownership interest and voting power held by the Company indirectly		Date of original acquisition	Proportion of shares originally acquired	Net consideration transferred <i>HK\$'000</i>
					30 June 2016	31 December 2015			
MACL <i>(note a)</i>	Development and commercialisation of jetpack products	New Zealand	Ordinary shares	245,294,108	52.01%	22.68%	23 February 2015	22.83%	83,237
Solar Ship <i>(note b)</i>	Development and commercialisation of solar powered aircrafts	Canada	Common shares	242,695	32.58%	32.58%	29 May 2015	32.58%	81,884
									165,121

As at the respective acquisition dates during the six months ended 30 June 2015, for the purpose of business expansion, the Company acquired 22.83% and 32.58% of the outstanding equity interest of MACL and Solar Ship respectively. In addition, as set out in more details in the notes below, as part of the acquisition agreements, the Company obtained rights to financial instruments containing potential voting rights to the Company for both investments (“the Conversion Rights”). Upon exercising these Conversion Rights, the Company’s shareholding in MACL and Solar Ship will be approximately 52.17% and 54.42% respectively, determined based on the number of shares in issue as at the respective acquisition dates and as at 31 December 2015. The dilution effect of the convertible debenture and outstanding share options issued by MACL and Solar Ship is insignificant to the Company’s shareholding in MACL and Solar Ship. As the Company has practical ability to exercise these Conversion Rights which gives the Company the current ability to direct the relevant activities of the respective investees, the directors of the Company consider the Company has control over MACL and Solar Ship. As a result, the Group applied the acquisition method in accounting for the acquisitions of MACL and Solar Ship.

Goodwill arose in these acquisitions because the considerations paid for the business combinations effectively included amounts in relation to the benefit of collaboration with the acquirees to develop cutting edge aviation and communication technologies which aimed at penetrating global markets. In addition, the Company could leverage on the acquirees’ experiences on integrating technologies in revenue driving business. These benefits are not recognised separately from goodwill because they do not meet the recognition criteria for identifiable intangible assets.

Acquisition-related costs arising from these acquisitions have been excluded from the consideration transferred and have been recognised as an expense during the year, within the administrative expenses line item in the condensed consolidated statement of profit or loss and other comprehensive income.

None of the goodwill arising on these acquisitions is expected to be deductible for tax purposes.

Notes:

- (a) On 19 December 2014, the Company and MACL entered into an investment agreement (“Investment Agreement”), pursuant to which upon MACL fulfilling certain conditions (“MACL Conditions”), the Company will (i) acquire up to 15,000,000 ordinary shares of MACL at an issue price of AUD0.40 per share from certain shareholders of MACL; (ii) subscribe for 40,813,636 new ordinary shares in MACL at an issue price of AUD0.40 per share; (iii) subscribe for convertible securities (“Convertible Securities”) that are convertible into 57,500,000 new ordinary shares of MACL at an issue price of AUD0.40 per share; and (iv) subject to the completion of the subscription of the new ordinary shares per (ii) above, the Company is to incorporate a company (“HKCo”) together with MACL in which the Company will contribute AUD2,000,000 (equivalent to approximately HK\$12,692,000) and will hold 51% of interest. At any time prior to 22 August 2017, the Company has the swap right (the “Swap Right”) to sell its 51% equity interest in HKCo to MACL which shall be satisfied by way of allotment and issuance of 89,250,000 MACL shares.

Pursuant to the Investment Agreement, as at 31 December 2014, the Company paid an interest bearing deposit on escrow (the “Deposit on Escrow”) for approximately AUD21,000,000 (equivalent to approximately HK\$133,277,000 as at 31 December 2014), where the deposit would be returned to the Company should MACL not meet the conditions set out in the Investment Agreement.

On 23 February 2015, the MACL Conditions were fulfilled. Accordingly, the Company subscribed for 40,813,636 new shares of MACL and acquired 14,950,000 existing shares of MACL for an aggregate amount of approximately AUD22,305,000 (equivalent to approximately HK\$135,200,000). The Deposit on Escrow was released upon the completion of the acquisition.

After the above acquisition and subscription of shares in MACL, the Company holds approximately 22.83% of the MACL’s issued share capital as at the acquisition date. The HKCo was incorporated on 12 March 2015 and both the Company and MACL have contributed AUD2,000,000 into the HKCo (approximately HK\$24,742,000 in total). As at 31 December 2015, the Company had the right to acquire but had not acquired the Convertible Securities and had the right to exercise but had not exercised the Swap Right.

The acquisition allows the Group to benefit from the aviation and flying technology of MACL for the development of the civil near space flying apparatus and the wifi broadcasting technology.

On 29 February 2016, the Company exercised its right to subscribe for the entire convertible securities in MACL for AUD23,020,000 (equivalent to HK\$129,988,000) and immediately fully converted them into new ordinary shares of MACL on the same date, the Group also exercised 90% of the Swap Right. The details are set out in note 13.

Fair value of assets acquired and liabilities assumed at the date of acquisition*HK\$'000*

Plant and equipment	3,881
Technical knowhow and patents for development and commercialisation of jetpack products	76,167
Other receivables	1,709
Bank balances and cash	167,043
Other payables	(20,076)
	<u>228,724</u>

The other receivables acquired in the transaction carried a fair value of HK\$1,709,000. The gross contractual amounts of those receivables acquired amounted to HK\$1,709,000 at the date of acquisition. None of the contractual cash flows are not expected to be collected at acquisition date.

Goodwill arising from acquisition**Total**
HK\$'000

Cash consideration transferred	135,200
Less: Fair value of derivative financial assets acquired	
– subscription right of Convertible Securities	(31,613)
– Swap Right	(20,350)
	<u>83,237</u>
Add: Non-controlling interests – share of net assets	171,962
Add: Non-controlling interests – share based payment reserve*	5,889
Less: Fair value of identifiable net assets acquired	(228,724)
	<u>32,364</u>

* As at the acquisition date, MACL had a share option scheme in terms of which share options over MACL's own shares were granted to its directors and employees. This share option scheme was not exchanged by the Group upon acquisition.

The non-controlling interests (77.17%) in MACL which represented present ownership interests in MACL recognised on acquisition date were measured at the proportion of the fair value of net assets of MACL attributable to the non-controlling interests.

Net cash inflow on acquisition of subsidiariesSix months ended
30 June 2015
HK\$'000

Consideration paid in cash	(135,200)
Add: bank balances and cash acquired	167,043
	<u>31,843</u>

MACL contributed no revenue and incurred a loss of HK\$7,365,000 for the period from the date of acquisition to 30 June 2015.

If the acquisition has been completed on 1 January 2015, total revenue of the Group for the six months ended 30 June 2015 would have been HK\$55,537,000 and loss for the six months ended 30 June 2015 would have been HK\$77,672,000. The pro forma information is for illustrative purposes only and is not necessarily an indication of the revenue and results of the Group that actually would have been achieved had the acquisition been completed on 1 January 2015, nor is it intended to be a projection of future results.

- (b) On 3 April 2015, the Company and Solar Ship entered into an investment agreement, pursuant to which upon Solar Ship fulfilling certain conditions (“Solar Ship Conditions”), the Company will subscribe for 79,070 new common shares in Solar Ship, representing approximately 32.58% of the outstanding common shares in Solar Ship for consideration of CAD 17,000,000. Also on the same day, the Company and Solar Ship entered into an option agreement, pursuant to which the Company was granted the option (“Option”) exercisable by the Company during the period from the completion of Solar Ship Conditions to 15 October 2016 (Toronto time) to subscribe for 116,279 additional common shares in Solar Ship for consideration of CAD25,000,000 (equivalent to approximately HK\$156,158,000), which will result in the Company holding approximately 54.42% of the outstanding common shares in Solar Ship. After negotiation between the Company and Solar Ship, it is agreed that the latest date for exercise the Option shall be extended to 15 January 2017 (Toronto time). The dilution effect of the convertible debenture and outstanding share options issued by Solar Ship is insignificant to the Company’s shareholding in Solar Ship.

On 29 May 2015, the Solar Ship Conditions were fulfilled. As a result, the Company subscribed for 79,070 new common shares in Solar Ship at the subscription money of CAD17,000,000 (equivalent to approximately HK\$106,085,000), representing 32.58% of the outstanding common shares of Solar Ship. As at the date that these consolidated financial statements were authorised for issue, the Company has the right to exercise, but has not exercised, the Option.

The acquisition allows the Group to benefit from Solar Ship’s aviation and flying technology for the development of Future technology business.

Fair value of assets acquired and liabilities assumed at the date of acquisition

	<i>HK\$’000</i>
Plant and equipment	7,289
Technical knowhow and patents for development and commercialisation of solar powered aircrafts	50,159
Other receivables	8,151
Bank balances and cash	93,997
Tax recoverable	712
Other payables	(13,056)
Obligation under finance leases	(147)
Convertible debenture	(7,393)
	<u>139,712</u>

The other receivables acquired in the transaction carried a fair value of HK\$8,151,000. The gross contractual amounts of those receivables acquired amounted to HK\$8,151,000 at the date of acquisition. None of the contractual cash flows are not expected to be collected at acquisition date.

Goodwill arising from acquisition

	Total <i>HK\$’000</i>
Cash consideration transferred	106,085
Less: Fair value of Option acquired	(24,201)
Net consideration transferred	81,884
Add: Non-controlling interests – share of net assets	87,951
Add: Non-controlling interests – share-based payment*	5,436
Add: Non-controlling interests – convertible debenture equity reserve	3,823
Less: Fair value of identifiable net assets acquired	(139,712)
Goodwill arising from acquisition	<u>39,382</u>

- * As at the acquisition date, Solar Ship had a share option scheme in terms of which share options over Solar Ship’s own shares were granted to its directors and employees. This share option scheme was not exchanged by the Group upon acquisition.

The non-controlling interests (67.42%) in Solar Ship which represented present ownership interests in Solar Ship recognised on acquisition date were measured at the proportion of the fair value of net assets of Solar Ship attributable to the non-controlling interests.

Net cash inflow on acquisition of subsidiaries

	Six months ended 30 June 2015 HK\$'000
Consideration paid in cash	(106,085)
Add: bank balances and cash acquired	93,997
	<u>(12,088)</u>

Solar Ship contributed no revenue and incurred a loss of HK\$2,018,000 from the date of acquisition to 30 June 2015.

If the acquisition has been completed on 1 January 2015, total revenue of the Group for the six months ended 30 June 2015 would have been HK\$55,537,000 and loss for the six months ended 30 June 2015 would have been HK\$77,872,000. The pro forma information is for illustrative purposes only and is not necessarily an indication of the revenue and results of the Group that actually would have been achieved had the acquisition been completed on 1 January 2015, nor is it intended to be a projection of future results.

Fair value measurements of financial instruments

Some of the Group's financial assets are measured at fair value at the end of each reporting period.

The following table gives information about how the fair values of these financial assets are determined (in particular, the valuation technique(s) and inputs used), as well as the level of the fair value hierarchy into which the fair value measurements are categorised (Levels 1 to 3) based on the degree to which the inputs to the fair value measurements is observable.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active market for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The following table gives information about how the fair values of these financial assets are determined (in particular, the valuation technique(s) and inputs used), as well as the level of the fair value hierarchy into which the fair value measurements are categorised (Levels 1 to 3) based on the degree to which the inputs to the fair value measurements is observable.

Financial instruments	30 June	Fair value as at	Acquisition date	Fair value hierarchy	Valuation techniques and key inputs	Significant unobservable input(s)		Acquisition date
	2016 HK\$'000	31 December 2015 HK\$'000				30 June 2016	31 December 2015	
(1) Subscription right of Convertible Securities	–	31,184	31,613	Level 3	Binomial Option pricing model is adopted and the key inputs are asset price, volatility, risk free rate, exercise price and discount rate in which the perpetual growth rate and discount rate are key inputs for the asset price	N/A N/A N/A N/A	Volatility: 44.63% Risk fee rate: 2.19% Discount rate: 17.95% Perpetual growth rate: 2% Exercise price: AUD0.4/share	Volatility: 33.42% Risk fee rate: 1.93% Discount rate: 19.7% Perpetual growth rate: 2% Exercise price: AUD0.4/share
(2) Swap Right	8,030	20,116	20,350	Level 3	Margrabe's Formula is adopted and the key inputs are swap assets price, correlation co-efficient and the volatilities of the swap assets in which the perpetual growth rate and discount rate are key inputs for the swap assets price	Volatility: 53.86% Perpetual growth rate: 2% Discount rate of MACL: 18.00% Discount rate of HKCo: 23.00% Correlation co-efficient: 0.5	Volatility: 44.63% Perpetual growth rate: 2% Discount rate of MACL: 17.95% Discount rate of HKCo: 22.74% Correlation co-efficient: 0.9	Volatility: 33.42% Perpetual growth rate: 2% Discount rate of MACL: 19.7% Discount rate of HKCo: 22.83% Correlation co-efficient: 0.9
(3) Option	N/A (note 1)	N/A (note 1)	24,201	Level 3	Binomial Option pricing model is adopted and the key inputs are asset price, volatility, risk free rate, exercise price and discount rate in which the perpetual growth rate and discount rate are key inputs for the asset price	N/A (Note: The option is recognised in equity and is not subsequently remeasured.)	N/A (Note: The option is recognised in equity and is not subsequently remeasured.)	Volatility: 33.36% Risk fee rate: 0.63% Discount rate: 26.6% Perpetual growth rate: 2% Exercise price: CAD215/share

Note 1: The option is recognised in equity and is not subsequently remeasured.

For all the financial instruments above, slight increases in the perpetual growth rates or volatility used in isolation would result in significant increases in the fair value measurement of the derivatives and vice versa.

21. CAPITAL COMMITMENTS

	30 June 2016 HK\$'000	31 December 2015 HK\$'000
Capital expenditure contracted for but not provided for in the consolidated financial statements in respect of the acquisition of plant and equipment	<u>9,761</u>	<u>13,108</u>

22. RELATED PARTY TRANSACTIONS

During the period, the Group entered into the following transactions with its related companies:

Name of related companies	Nature	Notes	Six months ended 30 June	
			2016 HK\$'000	2015 HK\$'000
New Spring Label	Sales of packaging products	(a)	–	14,427
	Management fee income	(b)	–	300
Beautiking Investments Limited	Rental expenses	(c)	90	90
New Spring Group Co., Ltd.	Rental expenses	(d)	54	108
REORIENT Financial Markets Limited ("REORIENT")	Advisory expenses	(e)	–	8,036

Notes:

- (a) The sale of packaging products was mutually agreed by the Group and the related company. There were no sales transactions for the six months ended 30 June 2016, as the Group ceased to do business with New Spring Label since June 2015.
- (b) The management fee income for the six months ended 30 June 2015 was charged on a monthly fixed amount mutually agreed by the Group and the related company.
- (c) The rental expenses paid were charged on a monthly fixed amount basis as mutually agreed by the Group and the related company. Mr. Ng and Ms. Li are the directors and the controlling shareholders of this related company.
- (d) The rental expenses were charged on a monthly fixed amount basis as mutually agreed by the Group and the related company. Mr. Ng and Ms. Li are the controlling shareholders of this related company.
- (e) The advisory expenses for the six months ended 30 June 2015 represent financial advisory services in respect of the transactions contemplated under the acquisition of Solar Ship and other financial advisory services. The terms of the non-recurring agreement were mutually agreed between the Group and the related company. REORIENT is ultimately a wholly-owned subsidiary of REORIENT Group Limited ("RGL") a listed company in the Stock Exchange and Mr. Ko Chun Shun, Johnson, an executive director and shareholder of the Company and RGL, is the controlling shareholder of RGL until 9 November 2015.

23. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with current period's presentation.

24. SUBSEQUENT EVENT

On 12 July 2016 and 17 August 2016, the Company received notices from the Subscribers respectively, to convert their respective fully paid preferred shares into ordinary shares at no extra consideration. Following the conversion of the above preferred shares, all the outstanding preferred shares were converted to ordinary shares and the Company has 6,089,401,125 ordinary shares.

MANAGEMENT DISCUSSION AND ANALYSIS

PERFORMANCE REVIEW AND PROSPECTS

The Group is principally engaged in (1) the research and development and manufacture of innovative products for future technology business, and the provision of other innovative technology service solutions (the “Future Technology Business”); (2) the manufacture and trading of paper packaging products and paper gift items and the printing of paper promotional materials (the “Paper Business”); and (3) the property investment. During the Period, the Group recorded a turnover of HK\$311,992,000, representing an increase of 462% over last year. Gross profit margin was up from 37.1% to 62.9%. Profit attributable by shareholders of the Company for the period increased to HK\$105,529,000, achieving a turnaround from loss for the Comparative Period. Basic earnings per Share increased to 1.85 HK cents.

The Future Technology Business – creating future smart cities

The Future Technology Business has been the focus of the Group. The Group has conducted the research and development of different disruptive technologies such as “future space” technology and “future artificial intelligence” technology, to provide comprehensive services and solutions. The Group is committed to creating future smart cities with the intention of solving all problems concerning city environment, convenience and safety.

During the period, the prime mission of the Future Technology Business was to develop space applications, under which the “in-depth space” technology was fully enhanced and extended to “future space” technology. Meanwhile, we continually diversified our future technology business groups to respond a brand-new business group constructed by a variety of future technologies and even sci-fic technologies for the development of future technologies.

Our “Future Space” products are combined with and use metamaterial technologies. They apply in wide-area internet-of-things networking, optical remote sensing and telemetry, internet access, smart big data collection, private network and backbone communication, smart observation, emergency rescue, transportation, space tourism and others, with the purposes of fully expanding human living space and enhancing the efficiency of space utilisation.

During the Period, revenue from the Future Technology Business was approximately HK\$284,732,000, representing an increase of 13 times over last year. Of the revenue, the “Cloud”, the Group’s fastest commercialised product, accounted for HK\$284,732,000. Selling and marketing expenses of HK\$20,902,000 and research and development expenses of HK\$49,766,000 were incurred for the products of the Future Technology Business. Together with other operating costs, segment profit for the Period was approximately HK\$107,833,000, achieved a positive turnover from the same period last year.

“Cloud” projects successfully commenced operation and space information platforms achieved stable operation

As at 30 June 2016, the “Cloud” project located in Dongguan base has operated steadily for more than six months. The platforms under the “Cloud” project regarding space information and loading were all in normal operation, providing important big data basis for city surveillance, ecological monitoring and fire warning. Meanwhile, the “Cloud” project located in Zunyi base has completed the system set-up and testing in full. At present, the “Cloud” has already been conveyed to the base headquarters for set-up and operation. Test flight will be conducted once the customer completed the construction of take-off base. Besides, the “Cloud” projects have gradually started running in the PRC cities and have successively entered into the design and implementation stages.

The “Cloud” is loaded with 400 kg of optical remote sensing and wide-area internet-of-things networking. The loaded optical remote sensing provides high resolution visual images of visible lights and infra-red rays. It is able to run 24/7 and can be used in road traffic monitoring in smart cities, inspection of unauthorised building works and wildfire detection. The internet-of-things networking covers areas with a diameter of 60 km and can be used in big-data collection and processing of smart information in smart cities. The “Cloud” has successfully set up a platform for collecting, distributing and processing city-level three dimensional in-depth information. It can be widely used in city planning management, ecological environment monitoring, meteorological forecast and monitoring, disaster forecast and assessment, marine ecological monitoring, wireless emergency communication, regional security and surveillance, and refined resource discovery, with the purpose of creating more eco-friendly and convenient smart cities.

The Group started to build the prototype of “Solar Ship” and conducted flying tests on completion of its design

During the period, the Group designed in general and detail certain models of “Solar Ship”, a low-level flying transport platform, followed by building prototypes and conducting flying tests. “Solar Ship” is a large and new-concept flying apparatus. In terms of design, it combines the technical features and edges of both airship and fixed-wing aircraft. It also integrates the design concept of solar clean energy system and idea of pure electric-powered green apparatus in achieving sustainable development. The product flies at altitudes between 1,000 meters and 3,500 meters, and has heavy loading capacity and long transport distance. It is also eco-friendly and has short take-off and landing.

Since 2016, the Group has started to build prototype and conducted flight tests for Solar Ship, which will be used in transportation, rescue and peacekeeping operations. The Group has now already teamed up with the related bodies of the Canadian government to further conduct progress flying tests and put into commercial operation of the latest version of the prototype. The prototype design proposal goes smoothly and is expected to carry out public testing and flight in 2016.

“KuangChi Martin Jetpack” started full safety tests and stepped further towards commercial use

“KuangChi Martin Jetpack”, the world’s first commercial and practical jet backpack, is the Group’s “black technology” product from the future. It is designed to accomplish a flying revolution for individuals. During the period, the Group also completed the testing, production and assembling of “KuangChi Martin Jetpack”. The Group aimed to complete the repeated safety tests of series I of “KuangChi Martin Jetpack” before delivery, so as to ensure its good performance for emergency rescue, police search and rescue, civil and commercial use, and high-end flying experience.

In order to cater for the customers’ demand on customisation and meet their expectation on the functionality of “KuangChi Martin Jetpack”, we have conducted repeated tests and examination on its safety systems such as automatic hovering system, ballistic parachute system and pilot protection structure. At the same time, not only have we consolidated and upgraded the overall performance of “KuangChi Martin Jetpack” in terms of technological characteristics including engine, power source, control and materials of the flying apparatus, but also reduced the costs of production and research of development. Series I of “KuangChi Martin Jetpack” is expected to commence commercial operation in 2017.

The near space tourism project is planned to take off this year

During the period, the Group began its design and development effort on the manned version of the “Traveller”, the key project for the Group’s near space business. The manned version of the “Traveller” is a new model of flying apparatus for near space tourism. It lifts and floats by helium and integrates aerospace grade life protection system. It is designed to meet the demand for near space tourism, and can be used for developing other scientific loading tests.

Since 2016, according to the original plan, the Group has completed the design of the tested manned version of the “Traveller”, as its functionally tested version, in general and as to its sub-systems. The Group has also checked the capsule hull and levitation system. According to the modification and test plans, the system assembling and reliability test are expected to complete soon. The Group will seek to carry out the launch and recovery tests in the second half of the year.

Innovative technologies were integrated and incubators were developed for industrialisation under the “Global Community of Innovation”

During the period, the Group was committed to creating the “Global Community of Innovation”. Under this “Global Community of Innovation”, there were a range of innovative technologies and platforms for industrialisation, that gathered innovators from all over the world to shoulder the innovation mission of “designing, realising and sharing the future”.

During the period, the “Global Community of Innovation” formally founded the “Incubator of Global Community of Innovation” (“GCI Incubator”) in Tel Aviv, Israel. The “GCI Incubator” is the first technology fund and incubator set up by Chinese technology enterprise in Israel. The total investment is US\$300 million, with the initial contribution amounting US\$50 million. The purpose is to make investments in technological innovation projects in Israel and the world.

Being a key member of “Global Community of Innovation”, KuangChi Science strives to promote the integration of innovative technologies and establishment of platforms for industrialisation. It also takes participation in the direct investment in innovation projects under the “GCI Incubator”. Ahead, KuangChi Science will incessantly fulfil the innovation mission to “plan, realise and share the future” along with the diversification of innovative technologies, the strengthening of research and development capabilities, the expansion of sales network and the improvement of product design and performance of the “Global Community of Innovation”.

Paper Business

During the Period, turnover contribution from the Paper Business dropped from HK\$35,220,000 for the Comparative Period to approximately HK\$27,080,000, resulting in a segment loss of approximately HK\$6,400,000 (Comparative Period: HK\$26,849,000). The Paper Business continued to suffer from the weakened global demand and fierce competition in the printing and packaging industry. The management will further tightened its cost control to improve its profitability. The initiatives will include simplifying production processes or outsourcing certain processes to subcontractors. On top of maintaining good relationships with existing customers, the Group will also attempt to promote its products and services to new customers so as to broaden its customer base.

Property Investment

The Group holds properties for investment purpose with a view to increasing its recurring rental income and capturing any possible future capital appreciation. During the Period, the Group recognised a rental income of approximately HK\$180,000 (Comparative Period: HK\$176,000), which remained at the similar level with the Comparative Period. Segment profit of approximately HK\$163,000 was generated (Comparative Period: HK\$167,000). The Group will closely monitor the conditions of the property market and be prepared to respond swiftly and take advantage of the market adversities to seize upon further suitable investment opportunities to provide tremendous value to shareholders.

Other Unallocated Corporate Income, Expenses and Finance costs

During the Period, interest income earned from fixed deposits and pledged deposits was approximately HK\$7,343,000 (Comparative Period: HK\$30,338,000).

During the Period, the unallocated corporate expenses of the Group significantly decreased from approximately HK\$49,202,000 for the Comparative Period to approximately HK\$27,452,000, primarily due to the legal and professional fees and the financial advisory expenses attributable to the acquisition activities of approximately HK\$14,500,000 during the Comparative Period.

Finance costs for the Period amounted to HK\$791,000 (Comparative Period: HK\$4,342,000), the decrease of which was due to full settlement of bank borrowings by the Group during the Period.

INTERIM DIVIDEND

The Board resolved not to declare any interim dividend for the six months ended 30 June 2016 (2015: Nil).

CAPITAL STRUCTURE

As at 30 June 2016, the Group had a registered and issued ordinary share capital of approximately HK\$57,137,000 and a preferred share capital of approximately HK\$3,757,000.

As at 30 June 2016, the Group did not have any bank borrowings (as at 31 December 2015: HK\$142,397,000).

LIQUIDITY AND FINANCIAL RESOURCES

As at 30 June 2016, the Group's total shareholders' funds amounted to approximately HK\$2,215,285,000 (31 December 2015: HK\$2,174,998,000). Total assets was approximately HK\$2,468,375,000 (31 December 2015: HK\$2,457,909,000) and total liabilities was approximately HK\$253,090,000 (31 December 2015: HK\$282,911,000).

As at 30 June 2016, the Group had bank balances and cash of approximately HK\$1,187,896,000 (31 December 2015: HK\$1,228,556,000) and the Group did not have any pledged deposits (31 December 2015: HK\$143,280,000). Gearing ratio, defined as the percentage of total interest bearing debts, which represented the convertible debentures of approximately HK\$6,396,000, to net asset value, was approximately 0.28% (31 December 2015: 6.81%, total interest bearing debts included the bank borrowings of HK\$142,397,000, the convertible debentures of approximately HK\$5,569,000 and the obligations under finance leases of HK\$233,000) as at 30 June 2015.

The Group's business operations and investments are located in the PRC, Hong Kong, New Zealand and Canada. As at 30 June 2016, bank balances and cash denominated in local currency and foreign currencies mainly included HK\$81,185,000, RMB298,221,000, USD88,438,000, NZD49,771,000 and CAD442,000 (31 December 2015: HK\$64,651,000, RMB601,286,000, USD81,397,000, NZD12,553,000 and CAD3,003,000) respectively. All the outstanding balances of borrowings and obligations under finance leases are denominated in HKD. Other than described above, most of the assets, liabilities and transactions of the Group are primarily denominated in HKD, RMB, NZD and CAD. The Group has not entered into any instruments on the foreign exchange exposure. The Group will closely monitor exchange rate movement and will take appropriate activities to reduce the exchange risk.

SIGNIFICANT INVESTMENTS, MATERIAL ACQUISITIONS OR DISPOSALS

Acquisition of subsidiaries

For the six-month period ended 30 June 2016, the Group did not have any material acquisitions or disposals. During the Comparative Period, the Group completed the acquisition of MACL and Solar Ship.

Details of the acquisitions have been disclosed in note 20 to the condensed consolidated financial statements.

On 29 February 2016, the Company subscribed for the entire convertible securities in MACL and fully converted them into new ordinary shares of MACL for AUD23,020,000 (equivalent to HK\$129,988,000). In addition, the Company also exercised 90% of the option for the allotment and issue of Swap Shares. The Company shall have the right to exercise the remaining 10% of the option prior to 22 August 2017.

After the allotment and issuance of new ordinary shares and Swap Shares of MACL, the Company holds approximately 52% of the enlarged issued share capital of MACL which, together with HKCo, continue to remain as subsidiaries of the Group. There is no net cash flows impact on the Group arising from these equity transactions.

KC Subscription in Longsheng

On 25 March 2015, Kuangchi Space Technology Company Limited (the “KCST”), a wholly owned subsidiary of the Company, and Zhejiang Longsheng Automotive Parts Stock Limited Corporation (浙江龍生汽車部件股份有限公司) (stock code: 002625.SZ) (“Longsheng”) entered into a subscription agreement (the “KC Subscription Agreement”), pursuant to which Longsheng conditionally agreed to issue, and the KCST conditionally agreed to subscribe for 41,958,041 new shares of Longsheng at the consideration of RMB300 million (equivalent to approximately HK\$375 million).

Longsheng will focus on the development of the smart structure and vehicle equipment in terms of intelligence, energy conservation and safety enhancement for the use in road transport and also the rail transit sector. The functions of these devices and equipment can be extended if they are connected to the internet, it enables the users to real time remote control the vehicles including the equipment installed in, perform traffic monitoring service and also provide big-data collection service and analysis. The Group focuses on disruptive spaces technology and services and its Cloud being able to provide Wi-Fi telecommunication, ground monitoring service and fly over remote areas. The Cloud can provide a practicable solution to allow the smart structure and vehicle equipment accessing the internet with minimum delay time to enable their online functions. The Directors considered that the smart structure and vehicle equipment will complement the current business of the Group.

Through this investment and the future possible cooperation between the Group and Longsheng, the Directors considered Longsheng would provide an opportunity for the Group to further penetrate the potential customers in the auto parts industry in the PRC.

On 15 April 2016 (after trading hours of morning session), Longsheng published an announcement on the website of Shenzhen Stock Exchange (www.szse.cn) in respect of the application of non-public issuance of shares of Longsheng has been approved by the Issuance Examination Committee of China Securities Regulatory Commission (the “CSRC”). As disclosed in the announcement, on 15 April 2016, the CSRC held a meeting to conduct an examination on the application of non-public issuance of shares made by Longsheng. Based on the results of the examination, the application of nonpublic issuance of shares of Longsheng has been approved. The Longsheng Shares subscribed by the Company pursuant to the KC Subscription Agreement are a part of the shares of Longsheng under the non-public issuance.

As Longsheng has not yet received the written approval documents issued by the CSRC, a separate announcement will be made by Longsheng upon receipt of the CSRC’s official approval documents.

Saved as disclosed above and disclosed herein this announcement, the Group did not have any other significant investment and there are no other material acquisition or disposal of subsidiaries and associated company during the Period.

CHARGES ON THE GROUP'S ASSETS AND CONTINGENT LIABILITIES

As at 30 June 2016, certain assets of the Group were pledged to secure banking facilities granted to the Group and obligation under finance lease as follows:

	30 June 2016 HK\$'000	31 December 2015 HK\$'000
Plant and equipment under finance leases	–	4,038
Pledged deposits	–	143,280
	<u>–</u>	<u>147,318</u>

As at 30 June 2016, the Group had no significant contingent liabilities (31 December 2015: Nil).

CAPITAL COMMITMENT

As at 30 June 2016, the Group has capital commitments as below:

	30 June 2016 HK\$'000	31 December 2015 HK\$'000
Capital expenditure contracted for but not provided for in the consolidated financial statements in respect of the acquisition of plant and equipment	<u>9,761</u>	<u>13,108</u>
	<u>9,761</u>	<u>13,108</u>

CORPORATE GOVERNANCE AND OTHER INFORMATION

Corporate Governance Practices

The Board acknowledges the importance of the highest standards of corporate governance as the Board believes effective corporate governance practices are fundamental to enhance the shareholders' value and safeguard the interests of the shareholders. Accordingly, the Company has adopted sound corporate governance principles that emphasis effective internal controls and accountability to all shareholders.

Throughout the period under review, the Company has complied with the code provisions of the Corporate Governance Code and Corporate Governance Report as set out in Appendix 14 to the Listing Rules (the "CG Code"), except for the deviations from the code provisions A.6.7 and E.1.2. Code provisions A.6.7 and E.1.2 stipulate that independent non-executive directors and chairman of the board of directors should attend the annual general meeting. Dr. Liu Jun, an independent non-executive director, and Dr. Liu Ruopeng, the chairman of the Board, did not attend the general meeting held during the Period owing to other business commitments. The Company periodically reviews its corporate governance practices to ensure that these continue to meet the requirements of the CG Code.

Code of Conduct Regarding Securities Transactions by Directors

The Company has adopted the Model Code as set out in Appendix 10 of the Listing Rules as its code of conduct regarding securities transactions by the directors. All directors have confirmed, followed by specific enquiry procedures by the Company, that they had complied with the requirements as set out in the Model Code throughout the Period.

Purchase, Sale or Redemption of Listed Securities

During the Period, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

Review of Interim Results

The interim results for the six-month period ended 30 June 2016 have been reviewed by the Company's Audit Committee and the external auditors, Deloitte Touche Tohmatsu, in accordance with the Hong Kong Standard on Review Engagements 2410 issued by the Hong Kong Institute of Certified Public Accountants.

On behalf of the Board
KuangChi Science Limited
Dr. Liu Ruopeng
Chairman and Executive Director

Hong Kong, 31 August 2016

As at the date of this announcement, the Board comprises four executive Directors, namely Dr. Liu Ruopeng, Dr. Luan Lin, Dr. Zhang Yangyang and Mr. Ko Chun Shun, Johnson; and two independent non-executive Directors, namely Dr. Liu Jun and Dr. Wong Kai Kit.